Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Petition for Forbearance From	)	
The Current Pricing Rules for	)	WC Docket No. 03-157
The Unbundled Network Element	)	
Platform	)	

OPPOSITION OF MCI

Mark D. Schneider	Kimberly A. Scardino
Marc A. Goldman	Lori E. Wright
JENNER & BLOCK	MCI
601 13th St., N.W.	1133 19th St., N.W.
Washington, D.C. 20005	Washington, D.C. 20036
(202) 639-6000	(202) 736-6478
MGoldman@Jenner.com	Kimberly.Scardino@mci.com

INTRODUCTION AND EXECUTIVE SUMMARY

Only months after this Commission announced that competitors will have continued access to UNE-P for mass market customers except where states make a finding of non-impairment, Verizon again argues that the Commission should effectively eliminate the availability of UNE-P. In what it designates a request for "forbearance," Verizon asserts that on UNE-P lines, the Commission should replace TELRIC rates with resale rates and deny competitors the right to provide access services, thus effectively eliminating UNE-P. Verizon bases its Petition on the same policy arguments it has made for seven years, hoping to win by dint of repetition a result it cannot obtain on the merits. The Commission should again reject Verizon's arguments, just as it did in the *Local Competition Order*, the *UNE Remand Order*, and in the Triennial decision itself.[1] Indeed, Verizon's policy arguments have even less force now that the Commission is reducing unbundling requirements with respect to broadband and is requiring states to eliminate UNE-P in those areas in which CLECs would not be impaired without it.

The bankruptcy of Verizon's *Groundhog Day* strategy is further apparent from the improper nature of its "forbearance" claim. The Petition does not actually request that the Commission forbear from regulating the rates at which the ILECs are compelled to offer facilities for lease. Not even Verizon is brazen enough to make such a request. Verizon instead argues for different pricing and unbundling rules than the Commission previously adopted. But that is not a request for forbearance at all. And even if it were an actual request for forbearance, Verizon's Petition does not meet the prerequisites for

[1] Our description of the Triennial decision is based on the Commission's press release.

forbearance under Section 10(a), as the existing rules are necessary to ensure that rates are nondiscriminatory, to protect consumers, and to protect the public interest. Moreover, under Section 10(d), the Commission has no authority to forbear from implementing the pricing requirements of Section 251 until the requirements of section 251(c) have been fully implemented. The Commission should not consider section 10(d) satisfied until it can conclude that in a relevant geographic area, a robust wholesale market exists that enables competing providers to obtain access to the telecommunications services and facilities they require to enter the market without the need for continued enforcement of Sections 251(c) and 271. As the Commission's Triennial Review ruling itself makes clear, that has not yet occurred. The Commission should therefore reject Verizon's request and consider any need for rule changes in an appropriate forum – such as the upcoming rulemaking on TELRIC rules.

In sum, we agree with NARUC that Verizon's petition should be rejected because: (1) a forbearance petition is not the appropriate vehicle to address general issues with TELRIC; (2) the merits of Verizon's petition depend on upcoming reviews of TELRIC and implementation of the Triennial Review; (3) the merits of Verizon's petition may vary from state to state, making national forbearance unwarranted, and (4) after six years of relative uncertainty, the Commission should not be radically changing the rules just after some certainty has been provided by the conclusion of legal challenges to TELRIC and the Commission's announced decision in the Triennial Review.

Table of Contents

Table of Authorities

FCC Orders	
1998 Biennial Regulatory Review	*1998 Biennial Regulatory Review*, Notice of Inquiry, 13 F.C.C.R. 21879 (1998)
Access Charge Reform Order	*Access Charge Reform: Price Cap Performance Review for Local Exchange Carriers: Transport Rate Structure and Pricing End User Common Line Charges*, 12 F.C.C.R. 15982 (1997)
CALLS Order	*Access Charge Reform: Price Cap Performance Review for Local Exchange Carriers: Low-Volume Long Distance Users: Federal-State Joint Board on Universal Service*, 15 F.C.C.R. 12962 (2000)
Local Competition Order	*In re Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, 11 F.C.C.R. 15499 (1996)
Massachusetts 271 Order	*In re Application of Verizon New England Inc., et al. for Authorization to Provide In-region, InterLATA Services in Massachusetts*, 16 F.C.C.R. 8988 (2001)
New Hampshire Delaware 271 Order	*In re Application by Verizon New England Inc., et al. for Authorization to Provide In-Region, InterLATA Services in New Hampshire and Delaware*, 17 F.C.C.R. 18660 (2002)
New Jersey 271 Order	*In re Application by Verizon New Jersey Inc., et al. for Authorization to Provide In-Region, InterLATA Services in New Hampshire and Delaware*, 17 F.C.C.R. 12275 (2002)
New York 271 Order	*In re Application by Bell Atlantic New York for Authorization under Section 271 of the Communications Act to Provide In-region, InterLATA Service in the State of New York*, 15 F.C.C.R. 3953, (1999), *aff'd*, *AT&T Corp. v. FCC*, 220 F.3d 607 (D.C. Cir. 2000)
NYNEX Order	*In re New England Telephone and Telegraph Company and New York Telephone Company Petition for Forbearance From Jurisdictional Separations Rules*, 12 F.C.C.R. 2308 (1997)
Pennsylvania 271 Order	*In re Application by Verizon Pennsylvania et al. for Authorization To Provide In-region, InterLATA Services in Pennsylvania*, 16 F.C.C.R. 17419 (2001)
Rhode Island 271 Order	*In re Application by Verizon New England Inc. et al. for Authorization To Provide In-region, InterLATA Services in Rhode Island*, 17 F.C.C.R. 3300 (2002)

Texas 271 Order	*In re Application by SBC Communications Inc., Southwestern Bell Telephone Company et al. Pursuant to Section 271 of the Telecommunications Act of 1996 to Provide In-region, InterLATA Services in Texas*, 15 F.C.C.R. 18354 (2000)
UNE Remand Order	*In re Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, 15 F.C.C.R. 3696 (1999)
State Commission Order	
NJ PUC Order	*In re Board's Review of Unbundled Network Elements Rates, Terms and Conditions of Bell Atlantic-New Jersey, Inc., Decision and Order*, Docket No. TO 00060356 (N.J. PUC Nov. 20, 2001)
PA Order	*Tentative Order, Generic Investigation Verizon Pennsylvania, Inc.'s Unbundled Network Element Rates,* R-000016683 (Oct. 24, 2002)
Other Materials	
Ordover Report	Ordover Report, attached to WorldCom Reply Comments in CC Docket No. 01-338 (FCC filed Sept. 3, 2003)
VZ Petition	Petition for Expedited Forbearance of the Verizon Telephone Companies, WC Docket No. 03-157 (FCC filed July 3, 2003)

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Petition for Forbearance From	)	
The Current Pricing Rules for	)	WC Docket No. 03-157
The Unbundled Network Element	)	
Platform	)	

OPPOSITION OF MCI

Verizon's Petition for forbearance should be rejected. Verizon is requesting rule changes, not forbearance – rule changes the Commission would have no authority to adopt even in a rulemaking proceeding. Its justifications for those rule changes have already been repeatedly rejected by the Commission, including most recently in the Triennial Review proceeding. Moreover, Verizon has not shown that its request meets the criteria for forbearance under Section 10(a), nor that *all* of the requirements for Sections 251(c) have been fully implemented, which is a prerequisite for forbearance under Section 10(d). Finally, Verizon's proposed rule changes are a prescription to return to monopoly telephone service, and could not be more at odds with the public interest or with the spirit and letter of the 1996 Act. Flash cut elimination of UNE-P would result in the end of local residential competition, reversing seven years of progress towards developing competitive local markets. And eliminating competition in the markets for exchange access now that the Bells have obtained long-distance entry in most markets similarly would spell the end to residential long-distance competition, setting the clock back decades further.[2]

To the extent that any changes to the current TELRIC rules are warranted, they should be made in the upcoming TELRIC docket that the Commission has indicated it intends to initiate. Verizon's attempt to obtain such rule changes in a forbearance petition is a cynical attempt to manipulate the time limits the Commission has to consider such changes and the substance of what the Commission will consider.

I. The Commission Lacks Authority to Implement Verizon's Requested Relief

A. Verizon's Petition Is Not A Request For Forbearance At All

Section 10 of the Communications Act authorizes the Commission to forbear from enforcing any regulation or provision of the Act when enforcement would be unnecessary and contrary to the public interest. Section 10 thus specifies circumstances in which the Commission has authority to free a carrier from particular requirements of the Act, including the FCC's implementing regulations. It does not provide the Commission free reign to adopt different rules in a proceeding that is not a rulemaking. But that is what Verizon requests the Commission to do here

Although Verizon casts its filing as a request for the Commission to "forbear from applying its current pricing rules to the UNE-P,"[3] that is not what Verizon actually requests. Forbearance would leave companies unregulated, free to charge any rate they

---

[2] The "me too" forbearance petitions of the other BOCs, *see* Joint Petition for Fobearance from the Current Pricing Rules for the Unbundled Network Element Platform, WC Docket No. 03-189 (filed July 31, 2003), should be rejected on the same grounds.

[3] Petition for Expedited Forbearance of the Verizon Telephone Companies, WC Docket No. 03-157, at 25 (July 3, 2003) ("VZ Petition").

choose for UNE-P, at least until states established new pricing rules. Not even Verizon has the temerity to make such a proposal. Verizon therefore morphs its request for "forbearance" into a request that the Commission *change* current rules, substituting avoided-cost for TELRIC (and for the statute's "cost-based rates" requirement) and prohibiting its competitors from using UNE-P to provide access services.

Whatever else one might say about these proposals, they are not appropriate requests for a forbearance petition, but rather require a notice-and-comment rulemaking that would involve the sort of detailed consideration of the appropriate rules that the Commission provided in the *Local Competition Order* and that it will again provide in its upcoming docket that reviews TELRIC rules generally. As the Commission has explained when rejecting an earlier forbearance petition, Verizon

> did not ask us merely to refrain from applying the current . . . rules. Instead, it proposed use of the Commission's forbearance authority as a means of replacing those rules with new ones without the notice and comment required by the Administrative Procedure Act . . . .[4]

That Verizon's request is not one for forbearance is also apparent from the types of policy arguments it makes. Verizon's arguments take two forms: (1) general attacks on TELRIC, and (2) general attacks on UNE-P. With respect to Verizon's general attacks on TELRIC, none of Verizon's arguments is unique to UNE-P. They are the very same arguments Verizon made against adoption of TELRIC in the first place, has made repeatedly since, and, presumably, plans to reiterate in the Commission's upcoming docket to consider revisions to TELRIC. They are arguments appropriate to that rulemaking, but have nothing to do with forbearance.

With respect to Verizon's attacks on UNE-P (its argument that CLECs should be relegated to resale rates for UNE-P and be foreclosed from providing access services), these are no different than the arguments Verizon made unsuccessfully in the Triennial. In that proceeding, Verizon argued that the Commission should find CLECs would not be impaired without access to unbundled switching for the very same reasons it uses here to justify relegating CLECs to resale rates. Once again, these are not forbearance arguments.

In sum, Verizon's Petition is a late-filed petition for rehearing of the 1996 Local Competition Order, a premature request for reconsideration of the Triennial, or an equally premature set of comments in the TELRIC docket. What it is not is a forbearance petition.

B. Verizon's Proposed New Rules Are Contrary To Law

Even if this were a rulemaking proceeding, not a forbearance proceeding, the Commission would not have authority to adopt the rule changes requested by Verizon, and such rule changes would be undesirable in any event. Verizon makes two specific proposals for changing the FCC's current rules governing UNE-P: the Commission should base prices for UNE-P on the avoided cost of retail local exchange services, pursuant to section 251(c)(4), and the Commission should prevent CLECs from being able to offer exchange access services over UNE-P lines. Verizon provides no policy justification for these specific proposals. Rather, they are based on its general policy arguments that TELRIC rates are "too low," and that *any* proposal that raised rivals'

---

[4] *See, e.g., In the Matter of New England Telephone and Telegraph Company and New York Telephone Company Petition for Forbearance From Jurisdictional Separations Rules*, 12 F.C.C.R. 2308 at ¶13 (1997).

costs would be beneficial. As will be shown below, Verizon's policy arguments are incorrect on their own terms. And they certainly do not justify the specific policy reforms Verizon proposes. In fact, these proposals are foreclosed by the Act. The Commission has no authority to implement these proposals in a rulemaking proceeding – much less in response to a forbearance petition.

1. *Verizon's Proposal of Resale Pricing Is Inconsistent with the Act*

Verizon's argument in favor of resale pricing for UNE-P is simply a request to eliminate UNE-P. Verizon recognizes this and thus attempts to resurrect the long-decided fight over the "all elements rule." Verizon contends that the Commission has discretion to reverse its prior conclusion that competitors can lease all of the elements needed to provide a service.[5] Verizon argues that the Commission therefore has discretion to allow leasing of all elements but at resale prices.[6] Both parts of Verizon's argument are incorrect, however, and in any event, would not provide a policy justification for the Commission to reverse its prior conclusions.

Requiring competitors to use some of their own facilities before they have a right to lease unbundled elements would be inconsistent with the statute. As the Commission explained in the *Local Competition Order*, "[t]he language of section 251(c)(3) . . . does not discuss, reference, or suggest a limitation or requirement in connection with the right of new entrants to obtain access to unbundled elements. . . . Congress did not intend section 251(c)(3) to be read to contain any requirement that carriers must own or control some of their own local exchange facilities before they can purchase and use unbundled

[5] VZ Pet. at 13.

[6] *Id*.

elements to provide a telecommunications service."[7] The Commission also rejected the requirement proposed by the ILECs based on four paramount policy considerations: (1) relegating carriers that could not use their own facilities to resale would limit them "to offering the same service an incumbent offers at retail," and limit their ability to "differentiate [their] products based on price" to "the margin between the retail and wholesale price of the product," (2) requiring carriers to use some of their own facilities would be "administratively impossible" because "it would not be possible to identify the elements carriers must own without creating incentives to build inefficient network architectures that respond not to marketplace factors, but to regulation," (3) requiring carriers to use some of their own facilities would likely be a requirement "so easy to meet it would ultimately be meaningless," and (4) requiring carriers to use some of their own facilities would artificially limit competition to those few markets that could "efficiently support duplication of some or all of the incumbent LEC's networks."[8] The Eighth Circuit upheld the FCC's conclusion that CLECs can lease combinations of unbundled elements used to provide a service, and the Supreme Court affirmed.[9]

Verizon does not challenge the Commission's justifications for the rules authorizing UNE-P, nor does Verizon directly propose that the Commission eliminate those rules. Instead, Verizon argues that the ostensibly discretionary nature of the Commission's decision authorizing UNE-P permits the Commission to adopt a different

7 *Local Competition Order* ¶ 328.

8 *Local Competition Order* ¶¶ 339-340.

9 *Iowa Utils. Bd. v. FCC*, 120 F.3d 753, 814 (8th Cir. 1997) ("plain language of subsection 251(c)(3) indicates that a requesting carrier may achieve the capability to provide telecommunications services completely through access to . . . unbundled elements,"), *aff'd in part and rev'd in part*, 525 U.S. 366, 392-93 (1999).

pricing standard for UNE-P than for individual elements – in this case the avoided-cost standard used for resale.[10] This does not follow, however, even if the premise of Verizon's argument were correct. The discretion the Commission has in determining whether CLECs would be impaired without access to a particular unbundled element does not mean the Commission has complete discretion on pricing once it has made a finding of impairment. Once the Commission has determined that transport must be unbundled, for example, the Act requires the ILECs to lease transport at cost. Similarly, the Commission's decision authorizing UNE-P, even if discretionary, subjects UNE-P to the requirement of cost-based pricing that applies to all unbundled elements. Because resale pricing is not a cost-based methodology, the Commission cannot apply this standard to UNE-P consistent with the Act's cost-based pricing provisions, and not just its own implementing regulations.

2. Verizon's Proposal is Impossible to Implement in Practice

The Commission cannot apply Verizon's standard to UNE-P for a more practical reason as well: it would be impossible to do so. One fundamental purpose of enabling competitors to lease unbundled elements is that they can provide services not offered by the ILECs. Because CLECs use combinations of unbundled elements to provide services not provided at retail by the ILEC, there will often be no retail service to serve as a baseline from which to determine a resale-like discount. In its Neighborhood product, for example, MCI offers a bundled product with specific combinations of features. The ILECs do not offer the same product. Thus, there would be no baseline product from which to calculate avoided cost, as the resale standard requires.

[10] VZ Pet. at 13-14.

3. *Verizon's Proposal for Revised Rules on Provision of Access Services Is Foreclosed by the Act*

The second rule change that Verizon proposes is to preclude CLECs from self providing exchange access services on UNE-P lines they have leased. Verizon proposes that a UNE-P CLEC that is providing interexchange service to its local customers will have to pay the ILECs access charges for long distance calls on those lines. This is a corollary to Verizon's position that CLECs should pay for UNE-P as if they were purchasing a resold service rather than leasing the line. But Verizon's proposed rule change would allow the ILECs to use price squeezes to eliminate long distance competition. Indeed, that would appear to be its obvious purpose. It would also be inconsistent with the Act's requirement of cost-based pricing.

In the *Access Charge Reform Order*, the Commission recognized that once the ILECs obtained long-distance authority pursuant to section 271 of the Act there would be a grave risk that the existing high access rates "create the conditions for an anticompetitive price squeeze when a LEC affiliate offers interexchange services in competition with IXCs."[11] The ILEC could charge high rates for access services over which it had market power, but charge low prices for long-distance services, forcing competitors either to lose money or lose customers – even if they were more efficient than the ILEC.[12] The Commission concluded, however, that:

> If an incumbent LEC does attempt to engage in an anticompetitive price squeeze against rival long-distance providers, the provisions of the Act should permit new entrants or other competitors to seek out or provide competitive alternatives to

[11] *Access Charge Reform: Price Cap Performance Review for Local Exchange Carriers: Transport Rate Structure and Pricing End User Common Line Charges*, 12 F.C.C.R.15982, ¶¶ 265-66 (1997).

[12] *Id*. ¶¶ 275, 277.

> tariffed incumbent LEC access services. For example, under the provisions of section 251, a competitor will be able to purchase unbundled network elements to compete with the incumbent LEC's offering of local exchange access. Therefore, so long as an incumbent LEC is required to provide unbundled elements quickly, at economic cost, and in adequate quantities, an attempted price squeeze seems likely to induce substantial additional entry in local markets. Accordingly, there should be a reduced likelihood that an incumbent LEC could successfully employ such a strategy to obtain the power to raise long-distance prices to the detriment of consumers.[13]

In sum, if interexchange carriers (IXCs) were faced with access charges that were too high, they would avoid those charges by competing in the local market.[14]

The precondition of the Commission's conclusion, however, was that an IXC could enter the market using unbundled elements and then would itself be able to self-provide access services, rather than having to pay access charges to the incumbent. If Verizon's proposed rule were put in place this precondition would no longer hold, and the price squeezes the Commission identified would immediately be implemented by the ILECs. As a result, long distance competition would be severely threatened. Verizon's proposal, in sum, is radically inconsistent with the Commission's long-standing policy governing access charges, and if adopted would toll the death knell for residential long-distance competition.

Verizon's proposed change in the rules governing exchange access would also violate the Act's requirements of cost-based pricing. Because TELRIC rates already provide the ILECs with "full compensation" for the lines they lease, enabling the ILECs to collect access revenues on UNE-P lines in addition to TELRIC rates would provide

13 *Id*. ¶ 280.

14 *Id*.

them with "compensation in excess of their underlying network costs."[15] This would be "inconsistent with the pricing standard for unbundled elements set forth in Section 252(d)(1)."[16] Moreover, the current rule under which CLECs collect the access charges furthers "Congress's overriding goal of promoting efficient competition for local telephony services, because it will allow, in the long term, new entrants using unbundled elements to compete on the basis of . . . economic costs."[17]

Verizon argues that the Act's requirement of cost-based rates does not preclude the Commission from permitting ILECs to collect access charges on UNE-P lines. Verizon says that experience shows that UNE-P rates do not permit incumbents to recover their costs. Even if that were true, which it is not, it would be an argument for adjusting the pricing rules to accurately reflect costs, not an argument for arbitrarily modifying the rules to enable ILECs to collect non-cost-based access charges in addition to TELRIC charges. Verizon makes no argument that the combination of TELRIC charges plus access charges would result in a cost-based rate. And contrary to Verizon's claim, permitting ILECs to recover both TELRIC rates and access charges would provide them with double recovery, as the current cost-based rates for unbundled elements are designed to enable ILECs to recover *all* of their costs associated with a line – including those of originating or terminating long distance calls on that line.

---

15 *Local Competition Order* ¶¶ 363 & n.772, 721.

16 In the *Local Competition Order*, the FCC adopted a plan that *temporarily* permitted ILECs to impose federal and state access charges upon new entrants because of the need for a transition from the existing regime. The Commission justified its decision, however, based on the need for a transition period from the existing regime, which it asserted was permitted by the Act. *Id*. ¶¶ 720-25. Now that the transition has occurred, however, no similar legal justification exists.

17 *Id*. ¶ 363.

Verizon's proposal that ILECs collect access charges on UNE-P lines is inconsistent with the Act for yet another reason: Verizon's proposal requires the Commission to adopt a different pricing standard for UNE-P than for unbundled elements generally. While the Commission could have adopted a different standard than TELRIC for assessing cost generally, it cannot adopt a different standard for UNE-P than for individual unbundled elements. A regime in which CLECs pay different amounts for UNEs depending on whether they are purchased individually or in combination is not one based on cost, when the added costs bear no relation to the cost of providing elements in combination.

Even if the Commission had discretion to permit ILECs to collect access charges on UNE-P lines -- and plainly it does not -- Verizon advances no persuasive policy reason for doing so. Verizon argues that access charges should flow to incumbents because the access charge regime was designed to support network infrastructure. This argument is not unique to access charge payments for UNE-P, however, and thus does not justify a special rule for UNE-P. It is also wrong. TELRIC rates fully compensate ILECs for their costs, including the costs of maintaining their infrastructure. Thus, there is no need for them also to receive access charge payments. If what Verizon means is that the current regime of switched access is a source of implicit subsidy for other services, the Commission has stated that it is not, and that a system of implicit subsidy is not sustainable in a competitive environment.[18]

Moreover, the Commission (and industry participants) fully understood that ILECs would not receive access charges on UNE-P lines at the time they established the level of access charges ILECs would receive. The Commission established the parameters of the current access charge regime in the *Access Charge Reform Order* and in the CALLS proceeding – *after* it had already established the rule that access charges would flow to the CLEC.[19] Allowing the ILECs to receive access charges on UNE-P lines would thus enable them to receive subsidies above and beyond those intended in the *Access Charge Reform Order* and in the CALLS proceeding and above and beyond those the Commission and industry participants felt were needed to support network infrastructure. As we explained above, the premise of the access charge reform that the Commission adopted was to the contrary that IXCs that entered the local market by leasing UNEs would not have to pay access charges. This was intended to help drive access charges to cost and to protect the long distance market against an anti-competitive price squeeze by the ILECs.

In sum, the changes Verizon proposes are unlawful and in many ways are directly contrary to explicit, long-held, and sound Commission policy.

II. Verizon's Petition Fails to Meet the Prerequisites for Forbearance Under Section 10

Even if one ignored the illegal nature of the relief Verizon requests, and even if Verizon's petition were one for forbearance, rather than a request for changes in existing rules, Verizon's forbearance petition still would have to be rejected because it fails to meet the prerequisites for forbearance under section 10 of the Act. Verizon's petition falls

---

18 *See Access Charge Reform Order* ¶ 404 (1997); *UNE Remand Order* ¶ 496 n. 994 (same).

19 *Access Charge Reform Order* ¶ 337 (1997); *Access Charge Reform: Price Cap Performance Review for Local Exchange Carriers: Low-Volume Long Distance Users: Federal-State Joint Board on Universal Service*, 15 F.C.C.R. 12962 (2000).

well short of the showing required to obtain forbearance relief under section 10(a). Verizon's petition is also barred by section 10(d), which precludes the Commission from forbearing from applying the requirements "of Section 251(c) or 271 . . . until it determines that those requirements have been fully implemented."

A. Verizon's Petition Does Not Satisfy Section 10(a)'s Test

Verizon's request that the Commission effectively eliminate UNE-P – by dramatically increasing the rates for UNE-P and restricting the use of UNE-P to local calls, would with the stroke of a pen wipe out the significant benefits that both local and long-distance competition is bringing to consumers. Verizon's Petition therefore fails to meet the requirements for forbearance set forth in Section 10(a), under which forbearance from enforcement of a regulation is appropriate only when the regulation is unnecessary to ensure charges are just and reasonable, when the regulation is unnecessary to protect consumers, and when forbearance would be consistent with the public interest. Section 10(b) states that in assessing the public interest, the Commission must evaluate whether forbearance "will promote competitive market conditions, including the extent to which such forbearance will promote competition among providers of telecommunications services." Here, the relief Verizon requests would have a devastating effect on competitive market conditions.

Verizon's argument that the Commission should price UNE-P at the avoided cost of retail local service and not permit CLECs to collect access charges is in effect an argument that CLECs should not be permitted to lease combinations of unbundled elements at TELRIC rates and, instead, should be relegated to resale. The Commission has repeatedly rejected this argument, including in its announced results in the Triennial

Review. The Commission was correct to reach this decision in the Triennial and earlier decisions and has even more reason to do so now.

As this Commission concluded in 1996, TELRIC is a widely accepted methodology for determining cost. It is indistinguishable from those prescribed in numerous state statutes and regulations mandating the use of forward-looking costs.[20] A forward-looking methodology is necessary to ensure just and nondiscriminatory rates, because under an alternative methodology, such as the avoided cost methodology proposed by Verizon, competitors would have to pay far more for access to facilities than would incumbents.

A forward-looking methodology such as TELRIC is also necessary to protect consumers and the public interest. The weight of expert economic testimony supports forward-looking methods such as TELRIC,[21] as does the 1996 Act's goal of transforming local telephone monopolies into competitive markets. TELRIC sends the correct price signals to potential market entrants, allowing them to build when it is more efficient to do so, and to lease when building competing facilities would be inefficient.[22] As Professor Janusz Ordover explains, "[w]hen TELRIC rules are properly applied, they will promote efficient entry and investment decisions by ILECs and CLECs, while enabling the ILEC to recover its investment in its network facilities."[23]

[20] *Local Competition Order* ¶¶ 671 & n.1675, 681 & n.1687.

[21] *Id.* ¶ 705; *see also* Ordover Report, attached to WorldCom Reply Comments in CC Docket No. 01-338 at 10 ("No one seriously disputes that the competitive marketplace values assets based on their forward-looking replacement value.").

[22] *Local Competition Order* ¶ 679.

[23] Ordover Report at 10.

These general justifications for TELRIC apply equally when TELRIC is used to price UNE-P. Relegating competitors to resale – or its equivalent through a resale-like pricing scheme – would not "promote competitive market conditions" under the standard for assessing the public interest set forth in Section 10(b), but would instead substantially diminish competition. As a matter of economic theory, it is TELRIC rates, not above-cost resale rates, that are intended to approximate those that a competitive market would produce. As a matter of empirical reality, it is only the availability of UNE-P at TELRIC rates that has led to the development of any significant competition in the mass market. Before regulatory decisions helped cement the availability of UNE-P at TELRIC rates, there was very little competition in the mass market. Even with UNE-P available at TELRIC rates, CLECs have struggled to gain significant market share. In New York, for example, the state in which competitors have gained the highest market share, CLECs have only achieved a 25% market share – counting all methods of competitive entry, and competitive gains in that state have now stalled.[24] If CLECs had to pay substantially more to lease unbundled elements, as they generally would at resale rates, CLEC market penetration would almost certainly diminish substantially. In no state, indeed in no pricing zone of any state, has resale provided an effective vehicle for local competition.

The relatively low level of CLEC market penetration helps show the fallacy of Verizon's claim that claim that CLECs have a 50-65% margin on UNE-P.[25] Verizon

---

[24] News Release, FCC, *Local Telephone Competition: Status as of December 31, 2002* at Table 6. After increasing from 9% to 23% between year-end 1999 and June 30, 2001, competitors' market shares increased only to 25% by December 31, 2001, and did not increase at all in 2002. *Id*. Competitors have not achieved even this level of success in other states. *Id*.

[25] *See* VZ Petition at 4 & n.6.

relies on a December 2002 Legg Mason report to support this claim, but the cited margin are simply the difference between the UNE-P price and the ILEC's retail rate.[26] Of course, in addition to purchasing UNEs, CLECs have a great many other expenses to cover in order to provide service. Those costs are significant as is apparent from the fact that later in the report, Legg Mason concludes that UNE-P is not a long-term threat even in the supposedly highly competitive market in New York.[27] Moreover, at least seven companies discontinued service in New York in 2001.[28] If CLEC margins were truly as high as Verizon claims, surely the data would reflect companies entering, not exiting, the market. Notably, the ILECs themselves have declined to enter out of region markets using UNE-P. The reality is that UNE-P has had significant but not overwhelming success to date, and would be far less successful if rates were increased substantially.[29]

A significant decrease in UNE-P competition would be directly contrary to the public interest, as even the limited competition that has already resulted from UNE-P has brought substantial benefits to consumers.[30] UNE-P has led to simpler rate structures, improved features, and lower rates, as well as protecting competition in downstream markets, such as the long-distance market. Before the advent of UNE-P, in states such as Pennsylvania, customers had a complicated "band" system even for purely local service.

---

[26] *See* Legg Mason, *UNE-P Relief: Investors Expect too Much* at 9 (Dec. 19, 2002).

[27] *Id.* at 16.

[28] *Id.* at 14.

[29] Verizon itself says that the reason many states have reduced UNE rates is to produce the "appearance of competition," Verizon Pet. at 3, implicitly acknowledging that when rates were significantly higher, competition did not develop either through UNE-P or resale. This is strong evidence of the likely result if CLECs were relegated to resale rates.

[30] *See* MCI Comments at 81-82; MCI Reply Comments at 134-35.

Through MCI's Neighborhood product, these customers now have access to the first bundled local/long distance product with calls free of charge to anywhere in the country, as well as an attractive combination of features. Z-Tel is offering customers products with unique features, unavailable from the BOCs.[31] Indeed, because CLECs using ILEC switches have access to the full functionality of the switch, they can design products with every bit the same creativity as if they were using their own switches.

UNE-P competition also has prompted the *ILECs* to offer new products and services to consumers. As one economic report explains, when CLECs enter a particular area using UNE-P, ILECs have been forced to respond by lowering prices and introducing expanded features of their own.[32] By producing better and less expensive phone service, TELRIC-based UNE-P ultimately fosters investment and economic growth, as the recent economic report concludes: "In addition to the direct benefit to individual customers, the availability of lower local phone service prices supports general economic development and employment – particularly in telecom-impacted industries, enhancing the overall competitiveness of the state in attracting and retaining investment and jobs."[33]

Finally, and equally important, UNE-P protects competition in downstream markets such as the long distance market and thus is vital to protect consumers and the

---

31 Z-Tel ex parte letter from Christopher Wright to Marlene Dortch, Triennial, CC Docket No. 01-338, Oct. 9, 2002, Attachment.

32 Lee L. Selwyn and Susan M. Gately, Economics and Technology, Inc., "Business Telecom Users Benefit from UNE-P-Based Competition" at 4-5 (Jan. 2003), *available at*: <http://www.econtech.com/UNE-P_Report.pdf> (discussing examples in five states); *see also* AT&T ex parte letter from Joan Marsh to Marlene Dortch in Triennial, Oct. 16, 2002.

33 *Id*. at 5.

public interest. In the absence of a vehicle by which competitors can profitably provide local service to mass market customers, the BOCs will be the only companies able to offer bundled local and long distance products. Market research shows that more than 50% of households in New York have the same provider for local and long distance. Approximately 90% of households ordering new service order a bundled product.[34] If the BOC is the only company that can offer such a product, long distance competition will quickly erode. Long distance competition will also erode because the BOCs will be able to impose price squeezes on their competitors, as we explained above. That would be directly contrary to the purpose of the Act under which section 271 was designed to maintain long distance competition by ensuring that local markets were open when the BOCs were providing long distance service. It also would be entirely inconsistent with the Act for the BOCs' to gain long distance entry based on provision of UNE-P at TELRIC rates and then be permitted to withdraw UNE-P from the market.

There is nothing on the other side of the ledger. As we show below in Part IV, the policy arguments Verizon presents in favor of forbearance are without merit. Thus, Verizon's Petition does not fulfill the requirements for forbearance established in section 10(a).

---

[34] Reply Decl. of Wayne Huyard in Triennial ¶ 18.

B. Section 10(d) Bars the Relief Requested by Verizon

Even if Verizon were able to meet the requirements of section 10(a), the Commission would have no authority to grant Verizon's requested relief because the petition fails to satisfy section 10(d). Section 10(d) of the Act states in relevant part that:

> the Commission may not forbear from applying the requirements of section 251(c) or 271 under subsection (a) of this section until it determines that those requirements have been fully implemented.[35]

The requirements of section 251(c) are continuing ones and cannot be said to have been fully implemented until Verizon loses its dominance in the local market in its region. Verizon still exercises market power such that the need to regulate the local market remains, as the Commission's Triennial decision makes clear. Thus, the Commission has no authority to forbear from applying the requirements of section 251(c).

Among those requirements is the requirement that unbundled elements be provided at cost-based rates. Specifically, Section 251(c)(3) requires incumbent LECs to provide access to unbundled network elements "on rates, terms and conditions that are just, reasonable and non-discriminatory in accordance with the terms and conditions of the agreement and the requirements of this section and section 252."[36] Section 252(d)(1)(A), in turn, requires that the rates for access to such unbundled elements "be based on the cost . . . of providing the . . . network element."[37] The FCC's regulations implementing section 252(d)'s pricing standard, in turn, define cost-based to mean in

---

35 47 U.S.C. § 160(d).

36 *Id.* § 251(c)(3).

37 *Id.* § 252(d)(1)(A).

accordance with Total Element Long Run Incremental Cost (TELRIC) pricing principles.[38]

The plain language of section 251(c)(3) thus unambiguously incorporates by reference the requirements of section 252, including the FCC's TELRIC pricing methodology. Section 10(d) thus prohibits the FCC from forbearing "from applying the requirements of section 251(c)" until those requirements have been "fully implemented."[39]

Verizon advances in a single, terse footnote two equally frivolous arguments in support of its claim that section 10(d) does not bar the forbearance relief requested in the petition.[40] First, Verizon erroneously claims that since "neither TELRIC nor UNE-P is required by the Act," they are not "requirements of section 251(c)" and, therefore, not covered by section 10(d) of the Act. Second, Verizon wrongly alleges that "once a carrier receives long distance in a given state, the Commission itself has concluded that those requirements [of sections 251(c) and 271] have been fully implemented."[41] Verizon's contention apparently is that a BOC that "has fully implemented the competitive checklist in [section 271(c)(2)(B)]" for purposes of obtaining in-region long

---

38 *See* 47 C.F.R. § 51.501 *et seq*.

39 47 U.S.C. § 160(d). *See, e.g., United States v. Ron Pair Enterprises, Inc.*, 489 U.S. 235, 240-41 (1989) ("where . . . the statute's language is plain, 'the sole function of the courts is to enforce it according to its terms.'") (citations omitted); *INS v. Cardoza-Fonseca*, 480 U.S. 421, 431 & n.12 (1987) (the "ordinary and obvious meaning" of a statutory phrase "is not to be lightly discounted") (citations omitted); *Chevron U.S.A., Inc. v. Natural Resources Defense Council*, 467 U.S. 837, 842-43 (1983) ("If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.").

40 *See* VZ Petition at 19, n. 38.

41 *See* 47 U.S.C. § 271(d)(3)(A)(i).

distance authority automatically has fully implemented *all* of the requirements of section 251(c) for purposes of section 10(d). Both of Verizon's claims are specious.

1. *The "Requirements" of Section 251(c) Include the FCC's Implementing Regulations.*

Verizon's cryptic assertion that "neither TELRIC nor UNE-P is required by the Act"[42] suggests that Verizon views section 10(d)'s bar as extending only to the text of section 251(c) itself, and not to the FCC's regulations implementing that provision. The Commission, however, has rejected that reading of the statute. In a 1998 notice in the *Biennial Review* proceeding, the FCC explicitly recognized that the term "requirement" in section 10(d) includes both "statutory provisions [and] the regulations implementing those provisions."[43]

Moreover, this reading of section 10(d) is consistent with the text of section 251 and prior statements by the Commission regarding the role of its local competition rules. Section 251(d)(1) of the Act directed the Commission to "establish regulations to implement the *requirements* of [section 251]."[44] In the *Local Competition Order*, the FCC indicated that it was adopting nationwide unbundling rules, including the TELRIC pricing regulations, pursuant to a "broad delegation of authority that Congress gave the Commission to implement the *requirements* set forth in section 251."[45] Thus, the

---

42 *Id.*

43 *1998 Biennial Regulatory Review*, Notice of Inquiry, 13 F.C.C.R. 21879, ¶ 32 (1998).

44 47 U.S.C. § 251(d)(1) (emphasis added).

45 *See Local Competition Order* ¶60 (emphasis added); *see also id.* ¶ 116 ("Section 252 generally sets forth the procedures that state commissions, incumbent LECs, and new entrants must follow to implement the *requirements* of section 251 and establish specific interconnection arrangements.") (emphasis added).

Commission's rules implementing section 251, including the pricing rules, clearly represent the agency's most authoritative statement of what that statutory provision requires.

Verizon also appears to suggest that section 10(d) does not apply to the TELRIC pricing rules, because they are not the only rules that the FCC could have adopted to implement sections 251(c)(3) and 252(d)(1) of the Act and, for that reason, are not "requirements" within the meaning of section 10(d). This argument, however, is simply a variation of Verizon's assertion that section 10(d) does not apply to the FCC's regulations implementing section 251(c). The Commission almost invariably has discretion in adopting rules that specify requirements of a particular statutory provision. If the precise requirements of the statute were clear, there would be no need for the Commission to enact implementing rules.[46]

In the instant case, the FCC, the expert agency charged with enforcing the Act, concluded that the TELRIC rules will achieve the statutory mandate of cost-based charges for access to unbundled network elements more effectively than any of the alternative pricing methodologies that were advanced in the section 251 rulemaking.[47] Thus, the current rules reflect the Commission's considered judgment regarding the specific ratemaking rules that must be followed to comply with that statutory requirement. The fact that a different Commission might have reached a different

---

[46] The Commission, for example, did not commence a rulemaking to specify the requirements of section 271. Rather, it simply determined on a case by case basis whether an applicant satisfied the statutory requirements.

[47] *Local Competition Order* ¶¶ 683-686 (comparing three pricing methodologies and determining that TELRIC is superior), *id*. ¶¶ 705-706 (rejecting embedded cost methodology); *id*. ¶¶ 709-711 (rejecting the "efficient component pricing rule" (ECPR)).

determination regarding the rules that would best implement the statutory provisions is irrelevant. Until modified after notice and opportunity for comment, the current pricing rules represent the expert agency's determination of the requirements of sections 251 and 252 and, therefore, are covered by section 10(d).

Moreover, because Verizon seeks to have the FCC replace the existing TELRIC rules with pricing rules that apply to resold retail services and do not relate to the underlying costs of the facilities involved, grant of its petition plainly would violate the statutory requirement that the charges for network elements be "based on the cost . . . of providing the . . . network element."[48] Thus, even under Verizon's untenable reading of the statute, section 10(d) bars the requested forbearance relief.

2. *Section 251(c) Has Not Been "Fully Implemented"*

Verizon's claim that section 10(d) does not bar the forbearance relief it seeks because it has fully implemented the requirements of section 251(c) is likewise without merit. Specifically, Verizon alleges that the Commission previously has found that the requirements of section 251(c) have been fully implemented when a carrier obtains in-region long-distance authority in a state.[49] To substantiate that claim, Verizon, however, does not cite an FCC order that contains such a statement. Rather, Verizon relies on a provision of section 271 which requires the Commission to find that a BOC "has fully

---

[48] 47 U.S.C. § 252(d)(1)(A). Verizon also asks that the FCC authorize the underlying facilities-based carrier to collect access charges for customers being served via UNE-P, rather than allowing the competitive carrier to collect those charges as the rules currently provide. For the same reasons discussed above, this request runs afoul of 10(d)'s prohibition against forbearing from section 252(d)(1)'s requirement that rates for network elements be based on costs. *See Local Competition Order* ¶ 363 (concluding that imposition of access charges in addition to cost-based charges for unbundled elements would depart from the statutory mandate of cost-based pricing of elements).

[49] *See* VZ Petition at 19, n.38.

implemented *the competitive checklist in [section 271(c)(2)(B)]"* in order to grant an application for in-region long-distance authority in a particular state.

Verizon thus confounds section 251 with section 271, and erroneously presumes that Congress intended to permit the FCC to refrain from enforcing the key market-opening requirements of the Act the instant that the Commission had determined that the BOC was actually complying with some of those requirements. This argument confuses what Congress required a BOC to show in order to gain in-region long distance authority with the showing required to satisfy section 10(d). Section 10(d) requires as a prerequisite of forbearance that a BOC fully implement *all* of the requirements of *section 251(c)*, including continuing obligations, not just those requirements on the section 271 competitive checklist. Moreover, because of the different purposes of sections 271 and section 10, even with respect to those requirements on the checklist, full implementation for purposes of section 10(d) requires more than a determination that the checklist has been satisfied. The forbearance provision of section 10 is only triggered, in the words of Senator McCain, "when markets are deemed competitive."[50]

As the Commission has held, section 271 requires a BOC seeking to obtain in-region long distance authority to show that it has *opened* its local markets to competitive entry.[51] But Congress did not require the BOCs to open their markets only to permit the BOCs immediately to close them again. Congress recognized that even after a BOC had satisfied the 271 checklist requirements and obtained in-region authority, it would

---

50 141 Cong. Rec. S7956 (June 8, 1995) (statement of Senator McCain) (quoting from Heritage Foundation letter).

51 *See, e.g., Texas 271 Order*, ¶¶ 1, 419; *New York 271 Order* ¶¶ 1, 15, 426, 428.

continue to be dominant in local telecommunications markets.[52] Consequently, Congress imposed on the Commission an ongoing obligation to ensure that a BOC continues to comply with the conditions it is required to satisfy to obtain section 271 approval, as well as the requiring each ILEC to continue to comply with the requirements of section 251. The Commission similarly has underscored the BOC's obligation to continue to comply with section 271 post-approval.[53]

Further, the Act and the FCC's section 272 implementing regulations establish safeguards designed to ensure that entrants would continue to have access under section 251(c) to the facilities and services they require to compete after a BOC's in-region entry.[54] Absent such continuing access, the Act's ultimate goal of fostering truly competitive local markets and deregulating the incumbent LECs could not be achieved.

It would have been completely irrational for Congress to have permitted the FCC to forbear from enforcing the requirements of 251(c) as soon as a BOC achieved interLATA authority, and it did not do so. Rather Congress required that prior to forbearance a BOC must fully implement *all* of the requirements of section 251(c), not just those on the competitive checklist.[55] The competitive checklist incorporates only

---

[52] 141 Cong. Rec. S8470 (June 15, 1995) (statement of Sen. Feingold) ("This checklist does not require that competition actually exist in local markets dominated by the RBOCs before they are able to use their substantial market power to enter long distance markets.").

[53] *See Texas 271 Order*, ¶ 434 (noting that "Section 271 approval is not the end of the road," that "[t]he statutory regime makes clear that [the BOC] must continue to satisfy the 'conditions required for . . . approval' after it begins competing for long distance business," and discussing "Congress's recognition that a BOC's incentives to cooperate with its local service competitors may diminish . . . once the BOC obtains section 271 approval.").

[54] *See* 47 U.S.C. § 271(d)(6)(A).

[55] See 47 U.S.C. 160(d).

subsections 251 (c)(2)-(4).[56] Critically, the requirements of section 251(c) include a variety of other vital continuing obligations. Section 251(c)(1), for example, requires that an ILEC negotiate in good faith. Section 251(c)(5) requires the ILEC to provide reasonable public notice of changes necessary for routing of services. A BOC has not fully implemented these continuing obligations just because it has received interLATA authority. Indeed, neither of these ongoing obligations under section 251(c) is incorporated in the competitive checklist. Thus, a BOC's showing in a section 271 application does not even implicate other provisions of section 251(c) that, according to Verizon, the Commission has discretion to forbear from enforcing.

Moreover, a Commission decision to grant a section 271 application does not mean that section 10(d) has been satisfied even with respect to those 251(c) requirements that are on the checklist. Sections 251 and the 271 checklist serve fundamentally different purposes. As explained above, section 271 is used to determine whether a BOC has sufficiently opened its markets at a fixed point in time that it can be permitted to offer in-region long distance services. Section 251, on the other hand, contains the critical unbundling obligations that often will remain necessary for the market to be competitive on a continuing basis.

The fact that both section 10(d) and section 271(d)(3) use the phrase "fully implemented" does not mean that Congress intended for that phrase to have the same meaning in both provisions. As the District of Columbia Circuit has noted, "[o]n numerous occasions, both the Supreme Court and this court have determined, after

---

[56] 47 U.S.C. § 271(c)(2)(B) (explicitly incorporating subsections 251(c)(2)-(4)); *see Texas 271 Order* ¶ *64* (implicitly incorporating subsection 251(c)(6) into subsection

examining statutory structure, context and legislative history, that identical words within a single act have different meanings."[57] In this case, the same two words appear in different Titles of the Act in provisions that, as discussed above, have very different purposes. Consequently, the most reasonable reading of section 10(d) is that a BOC's satisfaction of the statute's section 271 requirements falls well short of the showing required to meet the requirements of section 10(d).

As MCI previously has shown,[58] the most reasonable construction of the "fully implemented" requirement in section 10(d) is that it is satisfied, in the words of Senator McCain, "when markets are deemed competitive."[59] Specifically, the Commission should not consider section 10(d) satisfied until it can conclude that in a relevant geographic area, a robust wholesale market exists that enables competing providers to

---

271(c)(2)(B) by stating that the "provision of collocation is an essential prerequisite to demonstrating compliance with item 1 of the competitive checklist").

[57] *Martini v. Federal National Mortgage Ass'n*, 178 F.3d 1336, 1343 (D.C. Cir. 1999); *see also Atlantic Cleaners & Dyers, Inc. v. United States*, 286 U.S. 427, 433 (1932) (presumption that identical words in an act have the same meaning "is not rigid and readily yields whenever there is such variation in the connection in which the words are used as reasonably to warrant the conclusion that they were employed in different parts of the act with different intent"). Cases in which courts have assigned the same meaning to a word or phrase appearing more than once in a statute typically involve very different circumstances from those presented here. In a case involving a provision of the tax code, for example, the Supreme Court concluded that the term "overpayment" that appeared in different subsections of the same statutory provision should be given the same meaning in both subsections. *See Sorenson v. Secretary of the Treasury*, 475 U.S. 851 (1986). Moreover, in the *Sorenson* case, the subchapter in which both subsections appear included an explicit definition of "overpayment," thus "strengthen[ing] the presumption" that it has the same meaning throughout that subchapter. *Id.* at 860. Third, both subsections concerned the same subject matter, namely, treatment of overpayments. *Id.* None of these factors is present in the instant case.

[58] *See* Comments of WorldCom, Inc. on Verizon's Petition for Forbearance, CC Docket No. 01-338, at 12 (Sept. 3, 2002).

[59] 141 Cong. Rec. S7956 (June 8, 1995) (statement of Senator McCain) (quoting from Heritage Foundation letter).

obtain access to the telecommunications services and facilities they require to enter the market without the need for continued enforcement of Sections 251(c) and 271. Stated differently, the "fully implemented" standard requires a showing that a BOC no longer is dominant in the provision of the network elements and telecommunications services that entrants require to enter and compete effectively with the BOC.[60] The fact that section 10(d) applies to both section 251(c) and section 271 reinforces this reading of "fully implemented." Congress crafted a special limitation on forbearance for sections aimed at ensuring the development of local competition.

The conditions for forbearance under section 10(d) have not yet been established. Indeed, as MCI demonstrated in its UNE Triennial Comments, most local markets remain tightly shut and CLECs continue to be critically dependent on leasing UNEs from the BOCs. As a result, section 10(d) prohibits the FCC from forbearing to enforce its TELRIC pricing rules.

III. Verizon's Arguments in Support of Its Petition are Without Merit

Even if the Commission were to ignore the many legal infirmities that bar the relief Verizon requests, the policy arguments that Verizon provides to support its petition could not be more wrongheaded, and would not support that relief in any event. Verizon argues that the availability of UNE-P at TELRIC rates is harmful because: (1) it negatively affects BOC profits; (2) it decreases the incentive of the BOCs to deploy

---

[60] In interpreting the "fully implemented" language, it bears repeating that the requirements of section 10(d) are in addition to, not in lieu of, the section 10(a) standards that apply to any forbearance request. Under the latter provision, an applicant generally must show that the requested forbearance will not lead to unjust, unreasonable or unreasonably discriminatory practices by a carrier, will not harm consumers, and is consistent with the public interest. Congress, however, required something more before

facilities; (3) it decreases the incentive of CLECs to deploy facilities; and (4) it impairs development of a rational wholesale market. As we show below, these assertions are baseless. Indeed, the Commission concluded as a general matter in the Triennial Review proceeding that these identical policy arguments did not justify wholesale elimination of UNE-P. That remains true several months later. For the Commission to reach a different result today would be the height of arbitrary decisionmaking.

A. TELRIC Rates Adequately Compensate the ILECs

Verizon first argues that TELRIC undercompensates the ILECs. That argument is wrong, as the Commission previously concluded in a ruling that was affirmed by the Supreme Court. Verizon presents no significant new evidence here.

By calculating the rate for network elements on the basis of what it would cost to provide the functions the elements provide efficiently using up-to-date technology,[61] TELRIC "produce[s] rates for monopoly elements and services that approximate what the incumbent LECs would be able to charge if there were a competitive market for such offerings."[62] In a competitive market, "firms subject to competition from newer technologies (or from superior products) cannot ask their customers to support higher prices required for the recovery of the embedded costs of an old or inefficient technology."[63] By mirroring such a market, TELRIC enables incumbents "to recover a

---

it granted the FCC the discretion to forbear from enforcing section 251(c) (and section 271 as well).

[61] *Verizon Communications, Inc.. v. FCC*, 535 U.S. 467, 495-96 (2002).

[62] *Local Competition Order* ¶ 738.

[63] Ordover Report at 20. Thus, the price of a two-year old laptop is based on the price of a comparable new laptop, not the original purchase price of the old laptop. *Id*. at 20.

fair return on their investment" – including a reasonable profit.[64] Indeed, TELRIC enables incumbents to receive a higher return than would exist in a competitive market because TELRIC rates are reset only every three or four years despite continuing declining costs in the telecommunications industry, and because the Commission's TELRIC rules assume that existing wire center locations are fixed, whereas, in a competitive market competitors would be able to enter and place wire centers at the most efficient locations.[65]

Verizon responds that by pricing UNEs based on an efficient network that uses today's technology, TELRIC fails to compensate ILECs for the risks they take in installing technology that potentially will become outdated by subsequent technology. But "TELRIC does not assume that the actual telephone network is in fact competitive"; it "merely assumes a hypothetical competitive market as a means of designing the benchmark network and valuing the concomitant assets."[66] And TELRIC takes into account any risks of technological obsolescence by setting proper depreciation rates and costs of capital.[67] Verizon's criticism of TELRIC's calculation of the riskiness of investment is simply an abstract criticism of depreciation and cost of capital inputs that must be supplied in any cost model. This is a claim more appropriately made in specific cost proceedings. Indeed, for all it appears, Verizon is simply upset because its entirely

---

64 *Id*.; s*ee also id*. at 11 ("TELRIC-based rates are, by definition, designed fully to compensate ILECs in a manner consistent with the competitive standard for use of their network elements.")

65 *Verizon*, 535 U.S. at 504-06. *See also* Ordover Report at 17 (TELRIC models are conservative because they use existing wire center locations, because they build in excess capacity, and because they do not fully account for economies of scale and scope).

66 Ordover Report at 33.

67 *Local Competition Order* ¶¶ 686, 703; *Verizon*, 535 U.S. at 519-20.

unrealistic assumptions about such risk have been repeatedly rejected by state commissions once they have had the opportunity to review dispassionately all parties' evidence in these proceedings. For however Verizon's rhetoric may sound in the abstract, once the facts are examined Verizon's claims are rarely accepted. This is not because there is some conspiratorial growing systemic bias against incumbents in the cost proceedings in all 50 states, and it is not because there is some systemic flaw in TELRIC. It is because Verizon's claims are nothing but hot air.

Moreover, Verizon dramatically overstates the effects of the bottom up assumptions of TELRIC. In many respects, the network in a TELRIC model will not be that different from the embedded network, as most technology does not become outdated that quickly.[68] The bottom up nature of TELRIC is not intended to produce "low" rates. It is intended to result in a more reliable and transparent calculation than could be obtained by using the embedded costs found in the ILECs' books of accounts.[69]

Verizon suggests, however, that even if TELRIC theoretically provides adequate compensation to ILECs, it is not doing so in reality. But while Verizon and the other ILECs have had ample opportunity to establish that claim in concrete terms before state commissions, courts and this Commission over the last seven years, they almost never have even tried, and when state commissions have looked at the issue on their own, they have uniformly rejected this BOC claim as factually unsupported. [70] Verizon's support for the contrary conclusion is largely based on snippets of reports from a few analysts

---

[68] Ordover Report at 31 (largest component of network investment is outside plant, which has not dropped significantly in value).

[69] *Verizon*, 535 U.S. at 522.

who do little more than ape Bell press releases. [71] It is unclear what numbers or methodology these analysts are using for their calculations, however, and Verizon does not even attempt to make its case using its own reported data. It is just such analysts whose "independent" predictions regarding the strength of the telecommunications industry proved so inaccurate in the late 1990s, and MCI showed during the Triennial that the conclusions of these analysts are similarly incorrect regarding UNE-P.[72] Moreover, although Verizon quotes a report from JP Morgan, Verizon ignores JP Morgan's conclusion that BOC profitability will *increase* as a result of the bundled local/long distance products they can offer after section 271 entry.[73] In fact, Verizon recently reported solid second quarter results partly as a result of long distance gains it achieved as a result of 271 entry.[74]

---

70 Letter from Illinois Commerce Commission Chairman Kevin Wright to Senator Richard Durbin, Oct. 1, 2002.

71 VZ Pet. at 3. Verizon's claims that its margins are declining due to UNE-P are also suspect. *See* VZ Petition at 4. One of the studies cited by Verizon estimates that "as much as 84 percent of the decline in [BOC] margins in 2003 will come from pension-related costs." *See* Jo Maitland, Light Reading, *Bells Pinched by Pensions?* (Apr. 16, 2003), available at <http://www.lightreading.com/document.asp?doc_id=31406>. The second most important reason for the decline is "a shift from high-margin revenues of monopoly-like services to lower-margin revenues, such as data and long-distance services won in competitive markets." *Id.*

72 Letter from Donna Sorgi to Chairman Powell, Sept. 16, 2002.

73 JP Morgan, *Industries Face Off*, Sept. 16, 2002, at 8.

74 *TR Daily*, July 29, 2003. In any case, even if TELRIC rates are below the ILECs' booked costs, this may because of inaccuracies in ILEC numbers as a result of efforts to shift costs to the regulated portion of their activities, configuration of ILEC networks to produce a whole range of services, such as Centrex or future broadband video services, that are not part of the wholesale network, and inclusion of costs associated with providing retail services. Ordover Report at 41-46.

Verizon also claims that recent reductions in TELRIC rates show that the criteria for setting TELRIC rates are too subjective and permit states to set rates that are too low.[75] As the Supreme Court concluded, however, TELRIC is easier to apply than would-be alternative methodologies that depend on an evaluation of the ILEC's internal cost data.[76] Moreover, states have readily applied TELRIC to arrive at reasonable rates.[77] The recent reductions in TELRIC rates in many states actually result from laborious and careful costing proceedings. States have adjusted rates based on an increasingly sophisticated understanding of costs that did not exist at the time of the relatively hasty TELRIC proceedings that occurred in the wake of the *Local Competition Order*, and based on actual changes in costs that have resulted from technological changes or changes in network demand.[78] In fact, it is Verizon that convinced the D.C. Circuit that

---

75 VZ Pet at 2-3.

76 *Verizon*, 535 U.S. at 512, 522; Ordover Report at 23.

77 *Id*. at 522 (explaining that while "[a]t bottom, battles of experts are bound to be part of any rate setting scheme," it appears "that TELRIC rate proceedings are surprisingly smooth-running affairs").

78 The FCC has recognized that it is important to take such changes into account. *See Rhode Island 271 Order* ¶ 46 (explaining that it would be inappropriate to "forever freeze TELRIC proceedings and *de facto* fail to recognize increased sophistication in modeling or newly available evidence that could produce different, more precise TELRIC refinements that result in increased or decreased wholesale prices for UNEs"); *see also id*. ¶ 31 ("rates may well evolve over time to reflect new information on cost study assumptions and changes in technology, engineering practices, or market conditions."); *Massachusetts 271 Order* ¶ 35 (states are now able to set more accurate rates because "there has been significant guidance on what constitutes TELRIC-based rates from this Commission, other state commissions, and the courts. States may benefit from the experiences of other states that have undertaken extensive pricing analyses. Additionally, circumstances have changed since Massachusetts prices were originally set in late 1996. New developments, technologies, and information . . . have become available since that time.").

the existence of "rapid regulatory and technological change," meant that "rates may often need adjustment to reflect newly discovered information."[79]

Moreover, early rates were as often as not based on Bell inputs that misrepresented facts in devious ways that were not uncovered until years later. Verizon was one of the worst offenders in this regard, with its cost inputs embedded with double counting, misrepresentations about switch discounts, and every other kind of unreliable material. For example, the New York PSC initiated a review of Verizon's switching rates "in light of new evidence on switching costs. . . and the recognition that costs are continually changing in the evolving telecommunications industry."[80] After reviewing the new evidence, the New York PSC reduced Verizon's switching rates and adjusted other UNE rates as well. Similarly, in New Jersey, the PUC modified rates after asking the parties to augment the existing record by updating and revising their cost models to remove deficiencies previously found by the PUC and to reflect the current state of applicable law and regulation.[81] Far from being the product of whim, the PUC's subsequent decision to reduce rates was based on "an extensive record developed in an evidentiary proceeding that included 17 days of hearings, 26 experts witnesses, over 265 exhibits, and over 3,900 pages of transcripts."[82] Similarly, the Pennsylvania PUC has concluded in a Tentative Order that it should reduce UNE rates, and a final decision is

---

79 *AT&T v. FCC*, 22 F.3d 607, 617-18 (D.C. Cir. 2000).

80 NY PSC Press Release, *Commission Votes to Reduce Verizon's Wholesale Rates*, 02007/98C1357, Jan. 23, 2002.

81 *In re Board's Review Of Unbundled Network Elements Rates, Terms And Conditions Of Bell Atlantic-New Jersey, Inc., Decision and Order, Docket no. TO 00060356*, at 2 (Nov. 20, 2001).

82 *NJ PUC Order* at p. 2.

forthcoming. The Pennsylvania PUC reached this decision after holding several days of hearings, resulting in a lengthy transcript, as well as receiving numerous statements and exhibits.[83]

Verizon argues that in six states, Verizon was required during the section 271 process to reduce its rates to levels that benchmarked to the levels set in other states.[84] But as the FCC well knows, this is another Verizon fabrication. The FCC did not *require* Verizon to reduce its rates. To the contrary, the "benchmarking" Verizon complains of was a bone thrown to the BOCs by the FCC as a way to obtain section 271 authorization notwithstanding obvious material flaws in their cost inputs. Rather than simply deny the BOC applications because the pricing based on these flawed BOC inputs was not cost-based, over the objections of many commenters, including MCI, the Commission allowed the BOC applications to be granted if they would adopt rates that were analogous to rates accepted in other states. As the FCC stated, "[w]hen a state commission does not apply TELRIC principles or does so improperly (e.g., the state commission made a major methodological mistake or used an incorrect input or several smaller mistakes or incorrect inputs that collectively cold render rates outside the reasonable range that TELRIC would permit), then we will look to rates in other section 271-approved states to see if the rates nonetheless fall within the range that a reasonable TELRIC-based rate proceeding would produce."[85] For example, in the Rhode Island 271 proceeding, the FCC concluded that it could not find that Verizon had proven that its UNE rates were

---

[83] *Pennsylvania 271 Order* ¶ 4.

[84] VZ Pet., Att. B, para. 3.

[85] *Rhode Island 271 Order* ¶ 38.

adopted through a proceeding that correctly applied TELRIC principles; thus, it instead evaluated Verizon's rates based on a benchmark analysis.[86]

The flaw in this process was not that it resulted in a downward pressure on all rates; to the contrary, the result was that the *highest* rate that the FCC was willing to accept became the *floor* in future applications, as the BOC could reduce its rates to this floor and be assured of approval. The parties that have complained vigorously about "benchmarking" have been (until this petition) the competitive community, not the ILECs.

The parallel reductions in UNE rates in a number of states thus say nothing about whether these rates are now too low. Such adjustments are the expected result of a properly functioning rate setting process. And to the extent Verizon believes the rates are too low, its proper remedy is to convince the states to impose higher rates or to appeal the rates that have been put in place. Verizon also could have challenged these rates as confiscatory under the Takings clause, but has not done so, presumably because it realizes that the rates are fully compensatory.

---

[86] *Rhode Island Order* ¶ 32. Similarly, in the *NH/DE 271 Order*, the FCC expressed "serious concerns as to whether the New Hampshire Commission applied the proper interpretation of the TELRIC methodology in its SGAT proceeding," but did not need to address these concerns because Verizon, in the hopes of winning section 271 approval, relied in its application on reduced rates that would survive under the benchmark analysis. *NH/DE Order* ¶ 37. Had it not been for the benchmark test, presumably Verizon's applications in these and other states would have been rejected for non-TELRIC-compliant rates. Indeed, as the FCC notes, Verizon *chose* to rely on a benchmark comparison of its rates in RI and NJ to NY rates – they were not *required* to do so. *Rhode Island 271 Order* ¶ 39; *New Jersey 271 Order* ¶ 50.

B. The Availability of UNE-P at TELRIC Rates Does Not Deter Investment

Verizon alleges that the FCC's pricing rules in general, and their application to UNE-P in particular, have "contributed materially to the massive decline in investment in the telecommunications industry," "devalue[d] three quarters of the Nation's telecom infrastructure by two-thirds," and "undermined growth of the national economy."[87] The only "evidence" it presents for these extraordinary claims is the fact that total capital expenditures have declined since the investment boom in the 1990s.[88] Yet Verizon fails to present even the simplest of regressions to attempt to tie this decline to the availability of UNE-P at TELRIC rates, much less to present the complex analysis that would be needed to rule out the myriad number of far more obvious explanations as to why investment has declined. The most obvious of these are the downturn in the nation's economy since the beginning of 2000 and the realization among investors that telecommunications companies may have over-invested in facilities in the late 1990s, creating excess supply. There is simply no basis for Verizon's claim that the TELRIC pricing rules were a material cause of the economic decline. In fact, the evidence demonstrates that the TELRIC pricing rules have promoted investment by both incumbent and competitive carriers, and fostered facilities-based competition, even during these difficult economic times. Blaming the recent woes of the telecom sector, or the economy as a whole, on TELRIC is almost comical. But that is typical of the "analysis" Verizon offers up in this petition.

---

[87] VZ Petition at ii, 5 (citation omitted).

[88] VZ Petition at 7-8.

Verizon also fails even to attempt to take into account the impact of the Commission's Triennial Review Order, which will significantly modify the unbundling requirements. Under that Order, any potential for unbundling to negatively effect investment has been minimized, since facilities that competitors could economically build or lease in an unregulated market are no longer available for lease at a regulated rate. For example, there is simply no credible case that the availability of unbundled loops at TELRIC rates will deter BOC investment in loop upgrades now that the Commission is providing significant broadband relief.

Before turning to the specific evidence on the effect of TELRIC on investment, however, it is important to inject a note of caution. Verizon's argument wrongly assumes that facilities-based competition should be the single, overriding objective of the Commission's telecommunications policy. In many cases, however, it would be inefficient to induce competitors to invest in additional facilities.[89] Due to declining demand for second lines, for example, ILECs currently have excess capacity on many of their switches, and there is no reason to believe this excess capacity will soon be used up. Moreover, there is a chance that future developments in switching technology, such as packet switches, will replace circuit switches as the technology of choice. When there is excess capacity on the circuit switches already in place, it would be economically wasteful to attempt to induce CLECs to install their own circuit switches, even if regulation could induce such purchases. One of the important advantages of TELRIC is

[89] *See* Ordover Report at 11 ("[I]f, because of economies of scale and scope, the benefits of leasing at efficient rates exceed the costs of self-provision, leasing best serves the public interest. If the requesting carrier cannot satisfy its need for the element as cheaply as can the incumbent, then its facilities-based entry would waste resources. . . .")

that it induces CLECs to invest in their own facilities when it would be efficient to do so, but not otherwise.

1. *TELRIC Does Not Deter ILEC Investment*

As was the case with the evidence that Verizon presented in the Triennial, its argument that TELRIC rates discourage investment and harm the overall telecommunications industry borders on the frivolous. Verizon offers no probative evidence that TELRIC pricing has discouraged incumbent LECs from investing in facilities. Instead, Verizon merely points to a handful of analyst reports and articles estimating that investment by wireline carriers as a whole, including incumbent LECs, has sharply contracted since 2000.[90] Verizon fails to acknowledge, however, that such a trend (assuming the data are accurate) is much more likely the result of the severe economic slump that has plagued the entire U.S. economy during this same period – rather than the FCC's pricing rules. Indeed, after remaining stagnant for more than two years, corporate investment finally increased for the first time during the fourth quarter of 2002.[91] It is no more rational to attribute this increase in investment to the increased use of UNE-P in that quarter than to attribute the prior decline to such leasing – at least in the absence of further evidence.

Moreover, the record developed in the Triennial Review proceeding demonstrates, contrary to Verizon's unsubstantiated allegations, that the TELRIC pricing standard, far from deterring investment, actually *encourages* incumbent LECs to invest in

---

[90] VZ Petition at 6-8.

[91] *See* Jon Hilsenrath, "The Economy: U.S. Growth Waned in Fourth Period – GDP Increased Scant 0.7% As Defense Spending Helped To Fight Off a Contraction," *Wall Street Journal*, at A2 (Jan. 31, 2003), *available at*: <http://www-1.gsb.columbia.edu/courses/core/b6005/pressart/GDP_wsj2002Q4.pdf>.

facilities.[92] AT&T submitted evidence in that proceeding that "a 1% *reduction* in UNE rates corresponds with approximately 2.1% to 2.9% *increase* in ILEC investment."[93] Another study found that "UNE-P does not reduce and may instead increase RBOC investment."[94]

More recent studies further support this conclusion. Last month, the Phoenix Center for Advanced Legal and Economic Public Policy Studies released an empirical study that concludes that "UNE-P competition increases BOC net investment, with each UNE-P line increasing net investment by $759 per year."[95] This figure translates into about $5.2 billion in additional annual net investment in the BellSouth, SBC, and Verizon

---

[92] The Supreme Court reached a similar conclusion when it addressed a virtually identical argument by Verizon that TELRIC deters investment. Faced with evidence that incumbent LECs had invested "over $100 billion" during the four-year period after the Act, the Supreme Court dismissed such claims, concluding instead that TELRIC provides incentives for incumbent LECs "to invest and to improve their services to hold on to their existing customer base." *Verizon Communications Inc. v. FCC*, 535 U.S. 467, 517 n.33 (2002).

[93] Robert D. Willig, William H. Lehr, John P. Bigelow & Stephen B. Levinson, *Stimulating Investment and the Telecommunications Act of 1996* at ii (emphasis in original), attached to Letter from Joan Marsh, AT&T, to Marlene Dortch, FCC, CC Docket No. 01-338 (Oct. 11, 2002); *see also* Reply Comments of WorldCom at 155-56, CC Docket No. 01-338 (July 17, 2002) ("MCI Reply Comments"); Letter from Marc Goldman, counsel for WorldCom, to Marlene Dortch, FCC, at 11, CC Docket No. 01-338 (Nov. 13, 2002) (citation omitted) ("Goldman Letter"); Richard A. Chandler, A. Daniel Kelley & David M. Nugent, HAI Consulting, Inc., *The Technology and Economics of Cross-Platform Competition in Local Telecommunications Markets* at 90-96 (April 4, 2002) ("HAI Report") (the requirement that ILECs make UNEs available at economic cost does not reduce ILEC incentives to construct facilities), Attachment A to Comments of WorldCom, CC Docket No. 01-338 (April 4, 2002) ("MCI Comments").

[94] C. Michael Pfau, *Correcting the RBOCs' Empirical Analyses of the Linkage Between UNE-P and Investment* at 3, attached to Letter from Joan Marsh, AT&T, to Marlene Dortch, FCC, CC Docket No. 01-338 (filed Oct. 23, 2002) ("*Correcting the RBOCs*").

[95] Phoenix Center Policy Bulletin No. 5 at 13 (July 9, 2003) (analyzing data provided by ARMIS and UNE-P line data from FCC Form 477 for years 2000, 2001, and 2002).

regions.[96] By contrast, the Phoenix Center found that alternative forms of entry – UNE-L and Total Service Resale – had "no effect on BOC net investment."[97]

Finally, Verizon's assertions here are completely undermined by its own advocacy in the Triennial Review. In response to an analysis finding that investment by incumbent LECs was higher in those states where UNE-P was most prevalent, Verizon submitted a rebuttal report in which it compared the level of incumbent LEC investment with the level of UNE-P penetration in those 26 states in which competitive LECs had captured 10% or more of the access lines. Based on its analysis, Verizon concluded that "there is no statistically significant correlation between UNE-P and ILEC investment in [those] 26 states."[98] Verizon's rhetoric that UNE-P prices are the cause of recent BOC reductions in capital investment therefore must be dismissed as just that.

2. *TELRIC Does Not Deter CLEC Investment*

The record developed in the Triennial Review also refutes Verizon's claim that the availability of TELRIC-priced UNE-P discourages competitive LECs from investing in facilities. Evidence in that docket showed to the contrary that the availability of UNE-P would increase by 19% the rate at which competitive LECs deploy their own switches, while restrictions on UNE-P would decrease deployment.[99] Likewise, another study

---

96 *Id*. (calculation based on UNE-P lines in place in those regions in June 2002).

97 *Id*. at 14.

98 *UNE-P and Investment* at 12, Attachment C to Verizon Reply Comments, CC Docket No. 01-338 (July 17, 2002).

99 Z-Tel Comments at 80, CC Docket No. 01-338 (April 5, 2002); Z-Tel Policy Paper No. 4, *Does Unbundling Really Discourage Facilities-Based Entry: An Econometric Examination of the Unbundled Switching Restriction* (Feb. 2002), Attachment 9 to Z-Tel Comments; *see also* Phoenix Center Policy Bulletin No. 5 at 5 & n.10 (citing various studies disproving the claim that unbundling discourages investment by CLECs, and concluding that "there is no reliable econometric evidence of which we

concluded that there is no factual basis for concluding that UNE-P deters facilities-based competition.[100] In fact, that study found that, "everything else equal, there are *more* switch-based CLECs in states with *higher* than average UNE-P penetrations than in equivalent size states with lower than average UNE-P penetrations."[101] Verizon provides no new statistical analysis that contradicts the evidence presented in the Triennial, again relying primarily on its claims regarding diminished investment in the telecommunications sector as a whole.

In fact, recent evidence bolsters the conclusion that UNE-P does not diminish CLEC investment. FCC data regarding the state of local competition show that both the number of CLEC facilities-based lines (including both CLEC-owned and UNE-L) and the number of CLEC UNE-P lines increased steadily between December 1999 and

---

are aware that indicates unbundling discourages investment by either the BOCs or CLECs, or otherwise has any negative impact on economic performance in the telecommunications industry."); HAI Report at 88-90 (unbundling at economic cost does not reduce CLEC incentives to construct facilities); Goldman Letter at 11-15 (UNE-P does not decrease CLEC investment).

As with Verizon's argument regarding incumbent LEC investment, the Supreme Court also dismissed similar claims about the effect of TELRIC on CLEC investment, noting that those claims "founder[ed] on fact." *Verizon*, 535 U.S. at 516-17 (rejecting incumbent LEC "speculat[ion] that the investment has not been as much as it could have been under other rate making approaches" when faced with evidence that competitors had invested $55 billion since passage of the Act).

[100] *Correcting the RBOCs* at 2-3, 9. The study also concluded that "the degree of UNE-P penetration is not statistically different in states where facilities-based entry is present versus where it is not. Thus, there is no basis to conclude that greater UNE-P penetration deters facilities-based entry such as cable telephony." *Id.* at 13.

[101] *Id*. at 11 (emphasis in original).

December 2002.[102] Far from supplanting UNE-L, this trend suggests that UNE-P and UNE-L are complementary forms of entry.[103]

Verizon responds that the rate of growth in lines served by UNE-L that were "net adds" declined from 2000 to 2002 in eight states.[104] As an initial matter, Verizon's analysis confirms that, for six of these states, UNE-L has continued to grow, albeit at a

---

[102] The aggregate lines served by CLEC switches increased from 3.7 million to 10.7 million lines between December 1999 and December 2002. During the same period, UNE-P lines grew from 0.5 million to 10.2 million. *See* Industry Analysis and Technology Division, Wireline Competition Bureau, FCC, *Local Telephone Competition: Status as of December 31, 2002*, Tables 3 and 4 (June 2003) ("*2002 Local Competition Report*"). Verizon relies on the same data to claim that, between December 2000 and December 2002, "the number of CLEC-owned lines other than those provided through cable telephony decreased from 4.1 million to 3.4 million." VZ Petition, Attachment B at 20. This analysis, however, excludes growth in lines leased from incumbent LECs by competitive LECs that deploy their own switches. When those lines are included, the number of lines served by UNE-L CLECs or complete facilities-based CLECs (excluding cable) increased from 6.5 million in December 2000 to 7.7 million in December 2002. *See 2002 Local Competition Report* at Tables 3-5; Industry Analysis Division, Common Carrier Bureau, FCC, *Local Competition: Status as of December 31, 2000*, at Table 5 (May 2001). Thus, contrary to Verizon's claims, even when lines provided through cable telephony are excluded from the number of facilities-based lines, the FCC's statistics show that the number of lines served by UNE-L CLECs or complete facilities-based CLECs grew by over 18% between December 2000 and December 2002. Verizon's own petition confirms that the number of UNE-L lines increased during the first six months of 2002. *See* VZ Petition at 9 & n.23 (citing R.E. Talbot, RBC Capital Markets, Investext Rpt. No. 7229059, *Integrated Telecommunication Services – Moderating Expectations for* Triennial Review *– Industry Report*, at *13 (Feb. 18, 2003) (number of UNE-L lines rose from 3.7 million in the last half of 2001 to 4.1 million in the first half of 2002)).

[103] *See* Phoenix Center Policy Bulletin No. 5 at 5 (finding that the existing evidence "suggests a complementary relationship between UNE and facilities-based entry"); *see also* MCI Reply Comments at 154-55 (discussing fact that MCI and AT&T have built more switches in states in which UNE-P is available than in states that restrict access to UNE-P); *UNE-P: The Key to Local Competition* at 18-19, attached to Letter from Kimberly Scardino, WorldCom, to Marlene Dortch, FCC, CC Docket No. 01-338 (Oct. 2, 2002) (citing evidence that UNE-P has positive effect on UNE-L, and explaining that there is no evidence showing the absence of UNE-P increases UNE-L).

[104] VZ Petition, Attachment B at 16.

slower rate, over the past two years.[105] It, of course, is not unusual that UNE-L's rate of growth would decline as the customer base against which that growth is measured expands. In addition, Verizon's analysis completely fails to take into account other material factors, including, most notably, the sluggish economy and tight capital markets, that would likely contribute significantly to a slowing in the growth of UNE-L. In a related vein, Verizon claims that it filed evidence with the Commission in the Triennial Review demonstrating "that a number of carriers had begun to transfer lines off their own switches and onto UNE-P arrangements."[106] In fact, as NASUCA has pointed out, Verizon provided nothing save unverifiable statements to support this allegation.[107]

---

[105] Verizon's chart shows that use of UNE-L is actually contracting in two states in BellSouth's region, Georgia and Florida. In the case of Florida, the PSC has similarly reported that the use of UNE-L lines declined between 2001 and 2002; however, the PSC also found that, during the same time, the percentage of CLEC-owned lines increased from 39.4% to 50% of total CLEC lines. *See* Florida PSC, *Telecommunications Markets in Florida: Annual Report on Competition as of June 30, 2002* at 36 (Figure 16) (Dec. 2002), *available at*: <http://www.psc.state.fl.us/general/publications/reports/comptelemkt2002final.pdf> ("*2002 Florida Report*"). Other factors that likely have contributed to the declining use of UNE-L in BellSouth's region include the prevalence of integrated digital loop carriers (which for UNE-L providers typically result in higher non-recurring costs, longer installation periods, and inferior UNE-L service quality); continuing OSS difficulties; and targeted win-back activities. Finally, as a result of the general economic downturn, BellSouth itself has experienced declining growth in several of its services (unrelated to UNE-P). *See* Letter from Robert Blau, BellSouth, to Marlene Dortch, FCC, CC Docket No. 01-338, Attachment at 19 (Sept. 16, 2002) (BellSouth 9/16 Attachment) (noting that new voice line connections for its large business market were down 47% in the first half of 2002, and that hi-cap services for its carrier market declined from 33% growth in the first half of 2001 to -2.5% in the same period of 2002).

[106] VZ Petition at 9 & n.24.

[107] *See* Letter from Robert Tongren, President, NASUCA, to Chairman Powell, FCC, CC Docket 01-338, at 8 n.35 (Dec. 16, 2002) ("Verizon alone among the RBOCs has asserted – on a number of occasions – that some carriers have begun to convert customers from their own switches to UNE-P. Verizon has never provided any support for its statement.") (citations omitted).

Despite evidence of continuing growth in UNE-L lines, Verizon argues that investment in facilities by competitive carriers would be even more robust if UNE-P were not available.[108] Verizon presents no evidence to support this assertion, however.[109] And MCI and other carriers presented substantial evidence in the Triennial showing that the elimination of UNE-P generally would not lead to the establishment of UNE-L competition for mass market customers because of the economic and operational barriers CLECs face in using UNE-L. Indeed, as MCI has previously explained, experience has shown that limiting the availability of UNE-P does not lead to an expansion in the availability of UNE-L service for mass market customers.[110] Prior to 2000, there was little UNE-P competition anywhere in the country other than New York. Nevertheless, no significant competition for mass market customers using UNE-L developed during that period. Moreover, in areas of the country where the rates for unbundled switching limit UNE-P competition, UNE-L competition for mass market customers remains virtually non-existent.

---

[108] VZ Petition at ii, 2, 7-9.

[109] Verizon's claim that the percentage of business lines served by UNE-P has increased from 2001 to 2003, for example (VZ Petition at 10), does not show that the increase in UNE-P lines has led to a decrease in UNE-L (or pure facilities-based lines). The two analyst reports in support of its claim that UNE-P eliminates the incentive for competitors to build alternative local networks also show no such thing. *See id.* at 7 & nn.12-13. The first of those reports concludes that "a new national local network is unlikely to emerge" not because of UNE-P, but rather because of the natural monopoly in local services. *See* Bruce Roberts & William P. Carrier, Dresdner Kleinwort Wasserstein Research, *UNE-P: the Unprofitable RBOC*, at 2-3 (Aug. 9, 2002). The second report indicates that "UNE-P is not the primary problem for the RBOCs. . . . Technology substitution and economic weakness are far greater concerns." It adds that it was "never anticipated that the elimination of UNE-P would result in significantly increased spending levels by the local telecom carriers." *See* Gregory P. Miller & Chris Chapple, Fulcrum Global Partners, *Wireline Communications: Thoughts on FCC Order*, at 1, 5 (Feb. 25, 2003).

As for pure facilities-based competition, even Verizon does not have the temerity to claim that elimination of UNE-P would lead CLECs to construct their own loops to serve mass market customers. Verizon does suggest that the availability of UNE-P at TELRIC rates deters the development of cable telephony.[111] Again, however, Verizon presents no evidence to this effect, instead regurgitating quotations from a few analysts, as it did during the Triennial. Moreover, the very cable company Verizon says has been deterred by UNE-P[112] itself says that the recent growth in UNE-P had not led to a decrease in cable competition. "[W]e have not seen it [dampen sales] in any of our markets," explained Cox Communications President and CEO James Robbins. He added that this was in part because Cox's bundle of voice, data, and video service likely insulate it from churn caused by UNE-P.[113] And the BOCs themselves have argued that cable telephony has increased significantly in 2002 at the same time that UNE-P has increased dramatically,[114] thus substantially undercutting their claim that UNE-P is leading to a diminution in cable growth.

In any event, cable telephony serves such a small fraction of the market (less than two percent)[115] and the prospect of significant expansion in the near future is so bleak that any potential tradeoff between cable and UNE-P must be considered irrelevant. The HAI Report explained the many reasons that it is unlikely there will be a rapid expansion

---

110 Goldman Letter at 2.

111 VZ Petition at 10-11.

112 VZ Petition at 10.

113 *TR Daily*, Oct. 22, 2002.

114 *UNE Rebuttal Report* at 2.

115 *2002 Local Competition Report*, Table 5.

of cable telephony and none of these reasons have anything to do with UNE-P. Many of these were echoed in the presentation of Lara Warner at the Commission's en banc hearing in October 2002. She explained that there is little capital for facilities-based expansion of any sort, including cable, and that any spare capital available to cable companies will likely be devoted to defending their core video business.[116] The increase in cable telephony in 2002 discussed by the BOCs does not change this analysis. It still leaves cable with less than 2% of the residential and small business market.[117] That is not a basis for effectively eliminating UNE-P by ending the applicability of TELRIC rates.

In addition to being contradicted by all of the available empirical evidence, Verizon's claim that TELRIC discourages LEC investment in facilities is inconsistent with economic theory. Because TELRIC rates mirror rates that would exist in a competitive market, they provide competitors the proper incentive to build facilities. If the economic cost of serving customers on its own facilities is equal to or less expensive than the cost of serving customers using ILEC facilities (as measured by the cost-based rates set by the Commission), the CLEC would generally choose to use its own facilities. All other things being equal, CLECs have strong incentives to build their own facilities, rather than relying on UNE-P, because this would reduce the CLECs' reliance on their main competitor, the ILEC. If they do not do so, it is because of the economic and operational barriers to doing so, not because of TELRIC rates for UNE-P.

---

116 FCC en banc hearing, Oct. 7, 2002 (Tr. at 83-85).

117 WorldCom Comments at 35 (showing 1.5 million customers is less than 2 percent of residential and small business lines); *2002 Local Competition Report*, Table 5.

3. *TELRIC Does Not Undermine the Telecommunications Industry or the National Economy*

Verizon broadly claims that the application of TELRIC rules to UNE-P has harmed the telecommunications industry as a whole by deterring investment in new facilities and reducing market capitalizations. These effects, according to Verizon, have in turn retarded national economic growth.[118] Verizon's claims are without merit.[119]

First, as discussed above, TELRIC has not discouraged either incumbent or competitive LECs from investing in new facilities. To the contrary, the Phoenix Center has estimated that, from 1996 through 2001, the 1996 Act generated $267 billion in additional telecommunications investment from both incumbent and competitive LECs:

> From 1980 through 1995, investment by telecommunications firms grew at an annual rate of 2.8%, with average investment level of about $38.8 billion. After the 1996 Act, investment by telecommunications firms has grown at an average annual rate of 22.3%, with $95.3 billion invested annually (on average) for a total of about $572 billion during this time. Based on the difference between actual ($572 billion) and forecasted levels of investment ($305 billion), the 1996 Act is estimated to have generated $267 billion in additional telecommunications investment from 1996 through 2001.[120]

---

[118] VZ Petition at 5.

[119] In fact, the two sources that Verizon cites for the proposition that "the current pricing rules have contributed materially to a massive decline in telecommunications investment," *see* VZ Petition at 23, do not support its claim. The first source, a Brookings Institution Policy Brief, acknowledges the BOCs' argument that the FCC's pricing rules have discouraged investment and harmed the sector, but then expressly rejects those claims, noting that "the evidence points the other way." *See* Robert E. Litan, *The Telecommunications Crash: What to Do Now?*, Brookings Policy Brief #112 at 7 (Dec. 2002). The second source does not even mention the FCC or TELRIC, but rather blames the industry's woes on excess capacity outstripping demand and driving down retail rates. *See* Steve Rosenbush *et al.*, *When Will the Telecom Depression End?*, Business Week (Oct. 7, 2002).

[120] Phoenix Center Policy Bulletin No. 4 at 3 (June 24, 2003).

This level of investment far exceeded that predicted as a result of average annual investment prior to the Act.[121]

Second, the telecommunications industry clearly was not the only sector to experience a substantial decline in market capitalization since 2000. From early 2000 through October 2002, the stock market as a whole lost some $8.5 trillion in value.[122] The downturn in the global economy between 2000 and 2002,[123] not anything as specific and parochial as TELRIC-based UNE-P, is likely the biggest cause of the decline in the telecommunications industry.[124]

---

121 *Id.*

122 CNN Money, "Where Did the Money Go?" (Dec. 6, 2002), available at: <http://money.cnn.com/2002/12/06/pf/expert/ask_expert/> ("At the market's high back in early 2000, the market cap of the Wilshire 5000 totaled $17 trillion. By the time of the market's low in early October, the index's market cap had shrunk by about half that amount, or about $8.5 trillion."). The decline in market capitalization in the telecommunications sector fell most heavily on those firms attempting to enter local markets, not the BOCs. In fact, the stock prices of three of the four BOCs today remain above their 1996 levels, in stark contrast to those of competitive LECs, wireless providers, and long distance carriers. *See* Yahoo! Finance, Historical Prices, Monthly Historical Quotes from Feb. 1996 through July 2003 as adjusted for dividends and stock splits, for Verizon Communications (VZ), BellSouth Corp. (BLS), and SBC Communications (SBC), *available at*: <http://finance.yahoo.com/?u>.

123 *See, e.g.*, Standard & Poor's, Communication Equipment Makers to Reverse Two Years of Sharp Declines in 2003, Says S&P Equity Analyst in New Industry Study," *PR Newswire* (Aug. 7, 2003) Suzanne Kapner, "International Business: Nokia's Earnings Meet Expectations, While Ericsson Disappoints," *The New York Times* at C1 (Apr. 21, 2001); Maryanna Lewyckyj, "Dollar Dive Continues: Loonie Loss Caps Turbulent Trading Week," *The Toronto Sun* at 33 (July 27, 2002). The sources cited by Verizon confirm that the downturn in the telecommunications industry was not limited to the United States, *see* Steve Rosenbush *et al.*, *When Will the Telecom Depression End?*, Business Week (Oct. 7, 2002), and thus could not have possibly been due to UNE-P.

124 *See also* NARUC Letter to Sen. Daschle (Sept. 27, 2002) ("To the extent [BOC] returns are down for 2002, it may be attributable to the collapse of the capital markets, poor investment strategies, and perhaps some small and expected competitive inroads by competitors into the RBOC markets."); *id.* ("the loss of market share among monopoly providers is an expected outcome when successful competition public policies are implemented in the marketplace. It does not mean that the current UNE-P pricing

In short, Verizon's attempt to resurrect its Triennial arguments about the effect of UNE-P on investment must be rejected. The evidence it presents here is even less sophisticated than the evidence it presented in the Triennial. And it is also less relevant now that states can eliminate UNE-P altogether where CLECs can compete effectively without it. In any event, the best empirical evidence demonstrates that TELRIC pricing rules have actually encouraged investment by both incumbent and competitive LECs despite the economic downturn.

C. TELRIC Does Not Undermine the Development of a "Rational" Wholesale Market

Verizon finally claims that in the absence of TELRIC rules, the ILECs would continue to lease elements to CLECs because the ILECs would rather have the traffic stay on their network than end up on alternative facilities.[125] Verizon thus admits what should have been clear in any event: regardless of what actions the Commission takes with respect to its Petition, the effective elimination of UNE-P will not produce more facilities-based competition. If such competition were a real threat, the ILECs would lease their facilities at competitive rates in order to prevent facilities-based competition from developing.

Verizon's advocacy of facilities-based competition is thus just a smoke screen to argue that the "market," not regulators should set the price for leasing. The problem with

---

methodology is necessarily flawed, nor does it mean that the methodology is 'improperly applied' at the State level."); Legg Mason, Equity Research Company Update on Verizon Communications (Aug. 21, 2002), Attachment D to Letter from Donna Sorgi, WorldCom, to Chairman Powell, FCC, attached to Letter from Ruth Milkman, counsel for WorldCom, to Marlene Dortch, FCC, CC Docket No. 01-338 (Sept. 16, 2002) (concluding that Verizon's revenue stream is not endangered by UNE-P).

[125] VZ Petition at 11.

this argument is that facilities-based competition is not a real threat, as MCI showed in the Triennial. Thus, the absence of a requirement that ILECs lease elements at TELRIC rates would enable ILECs to refuse to provide access to UNE-P at any price – without any fear that such refusal would result in development of significant facilities-based competition. If any ILECs did lease unbundled elements, they would do so at rates far above those that would exist in a competitive market – thus limiting the extent of any competition that developed and substantially diminishing its benefits. Hence, the Commission should see Verizon's advocacy of "real" facilities-based competition as what it really is: a self-interested attempt to ensure that it faces *no* competition whatsoever.

CONCLUSION

For the foregoing reasons, Verizon's request for forbearance should be rejected.

Mark D. Schneider
Marc A. Goldman
JENNER & BLOCK
601 13th St., N.W.
Washington, D.C. 20005
(202) 639-6000
MGoldman@Jenner.com

Kimberly A. Scardino
Lori E. Wright
MCI
1133 19th St., N.W.
Washington, D.C. 20036
(202) 736-6478
Kimberly.Scardino@mci.com